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Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:PSI:B09

PLR-148203-06

Date:

April 10, 2007

In Re:

Legend:

Decedent	=
Spouse	=
Daughter 1	=
Daughter 2	=
Trust	=
Daughter 1's Trust	=
Daughter 2's Trust	=
Court	=
Date 1	=
Date 2	=

Dear :

This responds to a letter dated September 13, 2006 requesting rulings regarding the income, gift, and generation-skipping transfer (GST) tax consequences of the proposed division of a trust.

The facts submitted and representations made are as follows. Decedent died on Date 1. Date 1 is prior to March 1, 1984. Trust was established pursuant to the terms of Decedent's Will and First Codicil.

Article 4 of Trust provides that the residue of Decedent's estate is to be held in trust. Article 4.2 provides that during the lifetime of Spouse, subject to the trustee's discretion, Spouse is to receive distributions of income and principal to provide for her reasonable care, support, and comfort.

Article 4.3 provides that upon Spouse's death, subject to the trustee's discretion, income and principal are to be distributed to Daughter 1, Daughter 2, and their issue to provide for their care, maintenance, and health. Subject to the trustee's discretion, the issue of Daughter 1 and Daughter 2 are to receive distributions of income and principal to provide for reasonable expenses for their education. There is no requirement that the trustee equalize distributions among beneficiaries.

The Trust further provides that upon the death of the latter of Daughter 1 and Daughter 2, the trust estate is to be divided into equal shares, one for each living child of a deceased daughter, and each share is to be held in further trust. Each separate trust share held for a living child is to be distributed one-half to the child, free of trust, when he or she attains age 25, and the remainder of the trust share is to be distributed to the child, free of trust, when he or she attains age 30. If a child dies before the complete distribution of his or her trust share, the trustee is to distribute the remainder of the trust share as directed in a testamentary limited power of appointment. Assets not appointed are to be distributed among the child's living descendants, per stirpes, if any; and if none, among the Decedent's living descendants, per stirpes.

Spouse died on Date 2. It has been represented that all of the children of Daughter 1 and Daughter 2 are at least 30 years old. Daughter 1 and Daughter 2 each have four children.

The trustee intends to partition Trust into two trusts, Daughter 1's Trust and Daughter 2's Trust and amend Article 4.3 of Trust. The trustee of Trust has obtained the approval of Court for the division of the Trust and the amendment of Article 4.3. The Court order is contingent on receipt of favorable rulings from the Internal Revenue Service on the proposed modifications to Trust. Trustee has agreed to modify the Court order so that the following terms are in effect upon the division of Trust.

Amended Article 4.3 will provide that upon Spouse's death, the trust estate is to be divided into two trusts, Daughter 1's Trust and Daughter 2's Trust. Daughter 1's Trust and Daughter 2's Trust will have identical terms to Trust except for amended Article 4.3 and will have identical terms to each other except for the identity of the beneficiaries.

The amended terms of Daughter 1's Trust are as follows. Amended Article 4.3.A will provide that, subject to the trustee's discretion, income and principal are to be distributed to Daughter 1 and her children and Daughter 2 and her children to provide for their care, maintenance, and health. In addition, income and principal are to be

distributed to Daughter 1's and Daughter 2's children to provide for their education. There is no requirement to equalize distributions among beneficiaries.

Upon Daughter 1's death, Daughter 1's Trust is to be divided into equal shares, one share for each of Daughter 1's living children and distributed to each child, free of trust. If one of Daughter 1's children fails to survive until the complete distribution of his or her share, the trustee is to distribute the remainder of the share as directed in a testamentary limited power of appointment. Assets not appointed are to be distributed among the child's living descendants, per stirpes, if any; if none, among Daughter 1's living descendants, per stirpes, if any; and if none, among Decedent's descendants, per stirpes.

It has been represented that Trust has not yet been divided and that when Trust is divided, Trust's assets will be distributed on a pro-rata basis between Daughter 1's Trust and Daughter 2's Trust. It has been further represented that there have been no additions, actual or constructive, to Trust since its inception. The following rulings have been requested.

1. The proposed division of Trust into two successor trusts will not cause Trust to lose its exempt status under § 1433(b)(2)(A) of the Tax Reform Act of 1986 (Act), and § 26.2601-1(b)(1)(i) of the Generation-Skipping Transfer Tax Regulations, nor will the proposed division subject Trust or the resulting trusts to the GST tax.
2. The proposed division and pro-rata distribution of Trust into two successor trusts will not constitute a transfer of property by either Daughter 1 or Daughter 2 or subject either of them to the gift tax under § 2501.
3. The proposed division of Trust into two successor trusts and the pro-rata distribution of Trust's assets between the successor trusts will not result in the realization of any income under § 61 nor the realization any gain or loss under § 1001 by Trust or the beneficiaries.
4. After the proposed division of Trust into two successor trusts, the assets of the successor trusts will have the same basis under § 1015 as they had when held by Trust.
5. After the proposed division of Trust into two successor trusts, the holding periods of the assets held by the successor trusts will include the holding periods of the assets when the assets were held by Trust.
6. After the proposed division of Trust into two successor trusts, each successor trust will be treated as a separate taxpayer under § 643(f). Daughter 2's Trust will continue to use the current tax identification number of Trust and Daughter 1's Trust will receive a new tax identification number.

Law and Analysis:

Ruling 1:

Section 2601 imposes a tax on every generation-skipping transfer (within the meaning of Subchapter B).

Under § 1433(a) of the Act, the GST tax is generally applicable to generation-skipping transfers made after October 22, 1986. However, under § 1433(b)(2)(A) of the Act and § 26.2601-1(b)(1)(i), the tax does not apply to a transfer from a trust, if the trust was irrevocable on September 25, 1985, and no addition (actual or constructive) was made to the trust after that date. Under § 26.2601-1(b)(1)(ii), any trust in existence on September 25, 1985, will be considered irrevocable unless the settlor had a power that would cause the trust to be included in his or her gross estate under §§ 2038 or 2042, if the settlor had died on September 25, 1985.

Section 26.2601-1(b)(4)(i) provides rules for determining when a modification, judicial construction, settlement agreement, or trustee action with respect to a trust that is exempt from the GST tax will not cause the trust to lose its exempt status.

Section 26.2601-1(b)(4)(i)(D) provides that a modification will not cause an exempt trust to be subject to the provisions of chapter 13, if the modification does not shift a beneficial interest in the trust to any beneficiary who occupies a lower generation (as defined in § 2651) than the person or persons who held the beneficial interest prior to the modification, and the modification does not extend the time for vesting of any beneficial interest in the trust beyond the period provided for in the original trust. A modification of an exempt trust will result in a shift in beneficial interest to a lower generation beneficiary if the modification can result in either an increase in the amount of a GST transfer or the creation of a new GST transfer.

Section 26.2601-1(b)(4)(i)(E), Example 5, provides as follows. In 1980, Grantor established an irrevocable trust for the benefit of his two children, A and B, and their issue. Under the terms of the trust, the trustee has the discretion to distribute income and principal to A, B, and their issue in such amounts as the trustee deems appropriate. On the death of the last to die of A and B, the trust principal is to be distributed to the living issue of A and B, per stirpes. In 2002, the appropriate local court approved the division of the trust into two equal trusts, one for the benefit of A and A's issue and one for the benefit of B and B's issue. The trust for A and A's issue provides that the trustee has the discretion to distribute trust income and principal to A and A's issue in such amounts as the trustee deems appropriate. On A's death, the trust principal is to be distributed equally to A's issue, per stirpes. If A dies with no living descendants, the principal will be added to the trust for B and B's issue. The trust for B and B's issue is

identical (except for the beneficiaries), and terminates at B's death at which time the trust principal is to be distributed equally to B's issue, per stirpes. If B dies with no living descendants, principal will be added to the trust for A and A's issue. The division of the trust into two trusts does not shift any beneficial interest in the trust to a beneficiary who occupies a lower generation (as defined in § 2651) than the person or persons who held the beneficial interest prior to the division. In addition, the division does not extend the time for vesting of any beneficial interest in the trust beyond the period provided for in the original trust. Therefore, the two partitioned trusts resulting from the division will not be subject to the provisions of chapter 13.

In the present case, Trust was irrevocable on September 25, 1985. It is represented that no additions, actual or constructive, have been made to Trust after that date. Trust will be divided on a pro-rata basis into two successor trusts, and, except for the changes to Article 4.3, the successor trusts will have the same terms as Trust. The changes to Article 4.3 are similar to the changes described in § 26.2601-1(b)(4)(i)(E), Example 5. Therefore, the proposed division of Trust will not result in a shift of any beneficial interest in Trust to any beneficiary who occupies a generation lower than the persons holding the beneficial interests prior to the proposed division and the proposed division will not extend the time for vesting of any beneficial interest in Trust beyond the period provided for in Trust.

Accordingly, based on the facts submitted and the representations made, and provided the Court order is modified, we conclude that the proposed division of Trust into two successor trusts will not cause Trust to lose its exempt status under § 1433(b)(2)(A) of the Act, and § 26.2601-1(b)(1)(i), nor will the proposed division subject Trust, Daughter 1's Trust, or Daughter 2's Trust to the GST tax, provided there are no additions, actual or constructive, to Daughter 1's Trust and Daughter 2's Trust after September 25, 1985.

Ruling 2:

Section 2501 imposes a tax on the transfer of property by gift by an individual.

Section 2511 provides that the tax imposed by § 2501 applies whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible.

Section 2512(a) provides that, if a gift is made in property, the value thereof at the date of the gift shall be considered the amount of the gift.

In this case, the interest of each beneficiary will remain the same after the proposed division as it was prior to the division. Accordingly, based on the facts submitted and the representations made and provided the Court order is modified, we conclude that the proposed division and pro-rata distribution of Trust into two successor trusts will not

constitute a transfer of property by either Daughter 1 or Daughter 2 or subject either of them to the gift tax under § 2501.

Rulings 3:

Section 61(a)(3) provides that gross income includes gains derived from dealings in property.

Section 1001(a) provides that the gain from the sale or other disposition of property is the excess of the amount realized therefrom over the adjusted basis provided in § 1011 for determining gain, and the loss is the excess of the adjusted basis provided in § 1011 over the amount realized. Section 1001(c) provides that, except as otherwise provided, the entire amount of the gain or loss on the sale or exchange of property is recognized.

Section 1.1001-1(a) of the Income Tax Regulations provides, as a general rule, that except as otherwise provided in Subtitle A, the gain or loss realized from the conversion of property into cash, or from the exchange of property for other property differing materially in either kind or in extent, is treated as income or as loss sustained.

For purposes of § 1001, in an exchange of property, each party to the exchange gives up a property interest in return for a new or additional property interest. Such an exchange of property is a disposition under § 1001(a). See § 1.1001-1.

Rev. Rul. 56-437, 1956-2 C.B. 507, holds that a partition of jointly owned property is not a sale or other disposition of property where the co-owners of the joint property sever their joint interests in order to extinguish their survivorship interests.

An exchange of property results in the realization of gain under § 1001 if the properties exchanged are materially different. Cottage Savings Association v. Commissioner, 499 U.S. 554 (1991). A material difference exists when the exchanged properties embody legal entitlements “different in kind or extent” or if they confer “different rights and powers.” Id. at 565.

In this case, Trust’s assets will be distributed on a pro-rata basis between Daughter 1’s Trust and Daughter 2’s Trust. Accordingly, based on the information submitted and the representations made and provided the Court order is modified, we conclude that the proposed partition of Trust into two separate successor trusts to be funded on a pro-rata basis will not cause the interests of the beneficiaries of the separate trusts to differ materially. The beneficiaries will hold essentially the same interests before and after the pro-rata division. Therefore, the proposed division of Trust into two separate successor trusts will not result in the realization by Trust or the beneficiaries of any income under § 61 and will not result in the realization of any gain or loss under § 1001.

Ruling 4:

Section 1015 provides that the basis in property acquired by a transfer in trust is the same as it would be in the hands of the grantor, with adjustments for gain and loss recognized.

Section 1.1015-2(a)(1) provides that, in the case of property acquired after December 31, 1920, by transfer in trust (other than by a transfer in trust by gift, bequest, or devise) the basis of property so acquired is the same as it would be in the hands of the grantor increased in the amount of gain or decreased in the amount of loss recognized to the grantor upon such transfer under the law applicable to the year in which the transfer is made.

In this case, based upon the facts submitted and the representations made and provided the Court order is modified, we conclude that because neither §§ 61 and 1001 applies to the proposed transaction, the basis of the assets for each of the successor trusts will be the same as Trust's basis in the assets at the time of the transfer.

Ruling 5:

Under §§ 1223(2) and 1.1223-1(b), in determining the period for which the taxpayer has held property however acquired, there shall be included the period for which such property was held by any other person, if under chapter 1 of subtitle A such property has, for the purpose of determining gain or loss from a sale or exchange, the same basis in whole or in part in his hands as it would have in the hands of such other person.

Because § 1015 provides that the basis of the assets received by the successor trusts is the same as the basis of those assets in the hands of Trust at the time of the transfer, we conclude, based upon the facts submitted and the representations made and provided the Court order is modified, that, pursuant to § 1223(2), the holding periods of the assets held by the successor trusts will include the holding periods of the assets when the assets were held by Trust.

Ruling 6:

Section 643(f) provides that, for purposes of subchapter J of chapter 1 of subtitle A, under regulations to be prescribed by the Secretary, two or more trusts shall be treated as one trust if (1) such trusts have substantially the same grantor or grantors and substantially the same primary beneficiary or beneficiaries, and (2) a principal purpose of such trusts is the avoidance of the tax imposed by chapter 1.

Section 1806(b) of the Act provides § 643(f) shall apply to taxable years beginning after March 1, 1984; except that, in the case of a trust that was irrevocable on March 1, 1984, it shall apply only to that portion of the trust that is attributable to contributions to corpus after March 1, 1984.

Trust was established prior to March 1, 1984, and it has been represented that no additions have been made to Trust since its inception. Therefore, based on the facts submitted and representations made, we conclude that as long as Daughter 1's Trust and Daughter 2's Trust are separately managed and administered; they will be treated as separate trusts for federal income tax purposes.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Sincerely,

Melissa C. Liquerman

Melissa C. Liquerman
Senior Technician Reviewer
(Passthroughs & Special Industries)

Enclosures: Copy for § 6110 purposes

cc: